MATHEWS & FREELAND, L.L.P.

ATTORNEYS AT LAW

JIM MATHEWS
JOE FREELAND

P.O. BOX 1568
AUSTIN, TEXAS 78768-1568

(512) 404-7800
FAX: (512) 703-2785

June 12, 2009

Ms. LaDonna Castañuela
Office of the Chief Clerk
Texas Commission on Environmental Quality
P.O. Box 13087, Mail Code 105
Austin, TX 78711-3087

Re: Administrative Law Judges' Request to Answer Certified Questions; SOAH Docket No. 582-08-2863; TCEQ Docket No. 2008-0093-UCR; Appeal of the Retail Water and Wastewater Rates of the Lower Colorado River Authority; (1589.00; 4.1)

Dear Ms. Castañuela:

Enclosed, please find an original and seven copies of *Bee Cave's Brief on Certified Questions* for filing the captioned matter.

Sincerely,

Jim Mathews
Attorney for City of Bee Cave

JM/ndh
Enclosure

cc: Service List
Frank Salvato

SOAH DOCKET NO. 582-08-1700
TCEQ DOCKET NO. 2008-0091-UCR

PETITION OF RATEPAYERS APPEALING RATES ESTABLISHED BY CLEAR BROOK CITY MUNICIPAL UTILITY DISTRICT	§	**BEFORE THE STATE OFFICE**
	§	**OF**
	§	**ADMINISTRATIVE HEARINGS**

SOAH DOCKET NO. 582-08-2863
TCEQ DOCKET NO. 2008-0093-UCR

APPEAL OF THE RETAIL WATER AND WASTEWATER RATES OF THE LOWER COLORADO RIVER AUTHORITY	§	**BEFORE THE STATE OFFICE**
	§	**OF**
	§	**ADMINISTRATIVE HEARINGS**

SOAH DOCKET NO. 582-09-1168
TCEQ DOCKET NO. 2008-1645-UCR

PETITION OF WEST TRAVIS COUNTY MUNICIPAL UTILITY DISTRICT NO. 3 FOR REVIEW OF RAW WATER RATES	§	**BEFORE THE STATE OFFICE**
	§	**OF**
	§	**ADMINISTRATIVE HEARINGS**

BEE CAVE'S BRIEF ON CERTIFIED QUESTIONS

The City of Bee Cave is a petitioner in SOAH Docket No. 582-08-2863 (*Appeal of the Retail Water and Wastewater Rates of the Lower Colorado River Authority)*. Bee Cave files this brief pursuant to the notice from the Commission's General Counsel on May 15, 2009.

I. BACKGROUND LEADING TO CERTIFIED QUESTIONS

The certified questions presented to the Commission arise from three separate dockets that are procedurally and substantively distinct. These certified questions require the Commission to construe §49.2122 of the Texas Water Code enacted in 2007 and determine whether the Legislature intended by its enactment to fundamentally alter the Commission's obligation to ensure that retail public utility rates established by a district are just and reasonable. The Lower Colorado River Authority (LCRA) and the Executive Director contend that §49.2122 creates a presumption that rates set by a district are properly established for all purposes absent a

showing that the district's actions in setting the rates was arbitrary and capricious. Bee Cave disagrees, contending that the reach of §49.2122 is limited to the establishment of different charges among classes of customers.

Significant procedural and substantive differences between the three cases from which the certified questions arise are as follows.

SOAH Docket No. 582-08-1700 (Clear Brook City MUD)

Jurisdictional Basis:	Tex. Water Code §13.043
Rate Action Challenged:	Increase in water rates applicable solely to apartment classification.
Claims Asserted:	Rates are unreasonably discriminatory.
Ruling on §49.2122:	Section 49.2122 applies. District is relieved of the burden of proving that rates are just and reasonable until petitioner shows that district acted arbitrarily and capriciously.

SOAH Docket No. 582-08-2863 (LCRA Retail Rates for West Travis County System)

Jurisdictional Basis:	Tex. Water Code §13.043
Rate Action Challenged:	Change in retail water rates for all customer classes in West Travis County System.
Claims Asserted:	Revenue requirements are not just and reasonable. (Rate design allocating costs among customers within system is not challenged.)
Ruling on §49.2122:	Section 49.2122 does not apply. District has burden of proving that rates are just and reasonable

SOAH Docket No. 582-09-1168 (Travis County MUD 3 Challenge of LCRA's Contract Raw Water Rates)

Jurisdictional Basis:	Tex. Water Code §12.013
Rate Action Challenged:	Increase in raw water rate pursuant to contract.
Claims Asserted:	Revenue requirements are not just and reasonable. (Rate design allocating costs among customers is not challenged.)
Ruling on §49.2122:	No express ruling on applicability of §49.2122. Administratively Law Judge (ALJ) determined petitioner has burden of proof based on provisions other than §49.2122.

II. SUMMARY OF ARGUMENT

The Commission should not rule on these certified questions at this time because its ruling will constitute an advisory opinion that is not applicable to the pending contested case proceedings. The retail rates established in SOAH Docket Nos. 582-08-1700 & 582-08-2863 were adopted before Texas Water Code §49.2122 became effective and are not governed by its provisions. The contract raw water rates under review in SOAH Docket No. 582-09-1168 were not rates for retail water services and the Commission's jurisdiction was invoked under §12.013, not Tex. Water Code §13.043. Based on these factors the ALJ in that case has ruled that factors other than §49.2122 place the burden of proof on the petitioner.

If the Commission decides to answer these certified questions, the Commission should determine that Texas Water Code §49.2122 can be harmonized with Chapter 13 of the Water Code by interpreting this statute to apply only to allocations among customer classes, as the legislature originally intended. A determination that Texas Water Code §49.2122 creates a presumption that a district's rates are properly established for all purposes would create a direct conflict between Tex. Water Code §49.2122 and §13.043(j), which, pursuant to Tex. Water Code §49.002 would render §49.2122 inapplicable. Additionally, a determination that §49.2122 creates a presumption that a district's rates are properly established for all purposes could result in a significant decrease in the Commission's jurisdiction over districts and create unsettling implications for other areas of utility law.

III. THE COMMISSION SHOULD DECLINE TO ISSUE AN ADVISORY OPINION

As provided by the Code Construction Act, Tex. Govt. Code §311.022, "[a] statute is presumed to be prospective in its operation unless expressly made retrospective." Section 49.2122 applies prospectively to the act of a district in establishing "different charges, fees, rentals, or deposits among classes of customers." With respect to LCRA's water and wastewater rates for the West Travis County System, this action occurred in August 2007 prior to the September 1, 2007 effective date of §49.2122. Therefore, because new statutory language is presumed to have only a prospective effect, §49.2122 is not even applicable in Bee Cave's appeal. Similarly, the Clear Brook City Mud adopted the rates at issue in SOAH DOCKET NO. 582-08-1700 on August 9, 2007, also before the effective date of §49.2122. Finally, the rates at

issued in SOAH Docket No. 582-09-1168 are raw water rates pursuant to a written contract. The Commission's jurisdiction to set an appropriate rate was invoked under Tex. Water Code §12.013 rather than §13.043. Most importantly, the ALJ in that case has determined that provisions other than §49.2122 place the burden of proof on petitioner. Because of the specific facts of these cases, two of which relate to actions which occurred prior to §49.2122's enactment and one in which the burden of proof is controlled by provisions other than §49.2122, if the Commission answers the certified questions presented, the Commission would be providing an inappropriate advisory opinion.

IV. THE LEGISLATIVE INTENT IN ENACTING §49.2122 LIMITS ITS APPLICABILITY TO CUSTOMER CLASSIFICATION ISSUES

Texas Water Code §49.2122 was enacted in 2007 as an amendment to Senate Bill 3,[1] the omnibus water legislation for the 80th legislative session. Section 49.2122 provides as follows:

> Sec. 49.2122. *ESTABLISHMENT OF CUSTOMER CLASSES.*
>
> (a) Notwithstanding any other law, a *district may establish different charges*, fees, rentals, or deposits *among classes of customers* that are based on *any factor the district considers appropriate*, including:
>
> (1) the similarity of the type of customer to other customers in the class, including: [...]
>
> (2) the type of services provided to the customer class;
>
> (3) the cost of facilities, operations, and administrative services to provide service to a particular class of customer, including additional costs to the district for security, recreational facilities, or fire protection paid from other revenues; and
>
> (4) the total revenues, including ad valorem tax revenues and connection fees, received by the district from a class of customers relative to the cost of service to the class of customers.
>
> (b) A *district is presumed to have weighed and considered appropriate factors* and *to have properly established charges*, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously. (emphasis added)

This identical language was originally contained in HB 2301 filed by Rep. Robert Talton.[2] The caption of HB 2301 indicated that it was to be an act "relating to the authority of

[1] For information about this bill, see http://www.legis.state.tx.us/BillLookup/History.aspx?LegSess=80R&Bill=SB3.

certain special districts to establish *differences in rates between customer classes*." The bill analysis prepared for consideration of HB 2301 by the House Natural Resources Committee provided as follows:

> Currently, the water rate structure is unfairly different for *apartment complexes versus single family residences*. The fair establishment of water rates ensures that all the district's customers pay an equitable share of the expenses for the services provided by the district.
>
> HB 2301 would *allow a district to establish different fees among classes of customer* based on any factors the district considers appropriate.

Although HB 2301 was reported favorably without amendment from the House Natural Resources Committee to the Local and Consent Calendar, it was not considered on the House floor.[3] Instead, Representative Talton offered the language of HB 2301 as an amendment to Senate Bill 3. Floor consideration on Representative Talton's amendment was brief, to the point, and clear:

> SPEAKER: Following the amendment to the amendment, Clerk will read the amendment.
>
> CLERK: Amendment to the amendment by Talton.
>
> TALTON: Thank you Mr. Speaker. Members, this *just allows the districts*, the water districts *to do classes for billing rates*. I believe it's acceptable to the author. Move adoption.
>
> SPEAKER: Members, Mr. Talton sends up an amendment to the amendment. The amendment is accepted by the author. Is there objection? The chair hears none. The amendment in adopted.[4]

The bill became effective on September 1, 2007.[5]

On August 22, 2007, which was before the effective date of §49.2122, LCRA adopted rate increases for both water and wastewater utility services applicable to all customer classes in its West Travis County Regional System. Bee Cave appealed LCRA's water rates pursuant to Tex. Water Code §13.043(b). West Travis County MUDs 3 & 5 appealed both the water and

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[2] For information about this bill, see http://www.legis.state.tx.us/BillLookup/History.aspx?LegSess=80R&Bill=HB2301.
[3] See Texas Legislature Online, 80th Regular Session, HB 2301-Actions.
[4] See Texas Legislature Online, 80th Regular Session, Video Broadcast: House Chamber, May 22, 2007, from 3:49:28 – 3:50:03.
[5] See Section 14.01 of Senate Bill 3.

wastewater rates implemented by LCRA pursuant to Tex. Water Code §13.043(b). Bee Cave does not challenge LCRA's customer classifications within its West Travis County Regional System or the allocation of costs among those customer classes. Instead, Bee Cave challenges the reasonableness of LCRA's revenue requirements and the overall reasonableness of its rates. Bee Cave believes that LCRA's costs are unreasonable for the service provided.

V. RESPONSE TO CERTIFIED QUESTIONS

If the Commission chooses, to answer the certified questions posed despite its ruling constituting an advisory opinion, Bee Cave recommends that they be answered as follows.

1. Is Texas Water Code Section 49.2122 so inconsistent with Texas Water Code Section 13.043(j) that the two statutory provisions cannot be harmonized?

No, these two sections of the Water Code are not inconsistent when construed appropriately. If the two sections are construed to conflict, §49.2122 would be inapplicable because of the limitations on applicability expressed in Tex. Water Code §49.002. In this analysis, Bee Cave first reviews the interpretation of §49.2122 because this is the new section of statute which is in question.

A. Legal Principles Governing Statutory Construction

The fundamental principle of statutory construction is determination of the Legislature's intent. *Marcus Cable Associates v. Krohn*, 90 S.W. 3d 697, 706 (Tex. 2002).[6] The following language from a recent decision of the Texas Supreme Court clarifies that even when a statute is not ambiguous on its face, legislative intent should be ascertained and legislative history, titles, and context can and should be considered:

> We must construe statutes as written and, if possible, ascertain legislative intent from the statute's language. *Morrison v. Chan*, 699 S.W.2d 205, 208 (Tex.1985). *Even when a statute is not ambiguous on its face, we can consider other factors to determine the Legislature's intent, including*: the *object sought to be obtained; the circumstances of the statute's enactment; the*

[6] In *Marcus Cable Associates v. Krohn*, the Supreme Court construed Tex. Util. Code §181.102 to interpret the term "utility easement" to mean "public utility easement" based on statements made during committee consideration of the bill indicating legislative intent concerning the meaning of the term. 90 S.W. 3d at 706-707 (Tex. 2002).

> *legislative history*; the common law or former statutory provisions, including laws on the same or similar subjects; the consequences of a particular construction; administrative construction of the statute; and *the title*, preamble, and emergency provision. TEX. GOV'T CODE §311.023; *Ken Petroleum Corp. v. Questor Drilling Corp.*, 24 S.W.3d 344, 350 (Tex. 2000).
>
> Additionally, *we must always consider the statute as a whole rather than its isolated provisions. Morrison*, 699 S.W.2d at 208. *We should not give one provision a meaning out of harmony or inconsistent with other provisions, although it might be susceptible to such a construction standing alone. Barr v. Bernhard*, 562 S.W.2d 844, 849 (Tex. 1978). We must presume that the Legislature intends an entire statute to be effective and that a just and reasonable result is intended. TEX. GOV'T CODE §311.021(2), (3). (emphasis added).
>
> *Helena Chemical Co. v. Wilkins*, 47 S.W. 3d 486, 493, (Tex. 2001)

Based on the foregoing, any review of the plain language of §49.2122 must consider:

(1) the legislative history of the statute,

(2) the implications of the title for the section, and

(3) the entirety and context of the statute; *i.e.*, both subsections (a) and (b).

B. Legislative History

The legislative history underlying the enactment of Tex. Water Code §49.2122, summarized in Section IV above, provides a clear indication of legislative intent, expressed both in committee and on the house floor, that §49.2122 deals with to differing customer classes and their associated charges per class and nothing more. This legislative intent can be ascertained from:

(1) The caption of HB 2301 specifies that it is an act relating to authority of certain special districts to establish differences in rates between customer classes;

(2) The bill analyses prepared for HB 2301 consideration by the House Natural Resources Committee identifies a perceived problem concerning the establishment of rates for different customer classes and states that the bill's purpose is to authorized the establishment of customer classes; and

(3) Representative Talton's clear and concise statement to the House chamber upon consideration of his amendment that led to the enactment of Tex. Water Code §49.2122 that "this just allows the districts… to do classes for billing rates."

C. Section Titles

As recognized by the Supreme Court in *Helena Chemical Co.*, the Code Construction Act authorizes consideration of the title or caption of a statute in construing its meaning regardless of whether or not the statute is considered ambiguous on its face. Tex. Gov't Code §311.023(7). The titles used by the Legislature in enacting Tex. Water Code §49.2122 are a clear indication that its provisions are intended to address the subject of customer classes and nothing more. §49.2122 is the only section enacted under Article 7 of SB 3. Article 7 is entitled "Rate Classes for Billing." Section 49.2122 itself is entitled "Establishment of Customer Classes." These titles, used by the Legislature in enactment of §49.2122, are equally applicable to subsections (a) and (b), and must be given consideration in construing and harmonizing both sections.

D. Reading Subsections Together as a Whole

Subsection (a) of §49.2122 identifies appropriate factors for a district to consider when establishing different charges among classes of customers. Subsection (b), thereafter creates a presumption that the district weighed and considered "appropriate factors in establishing charges." The references to "appropriate factors" and "charges, fees, rentals, and deposits" in subsection (b) relate back to the factors and different "charges, fees, rentals, or deposits among classes of customers" first described in subsection (a). Subsections (a) and (b) must be read together in order to harmonize the legislative intent in enacting the statute. The only logical resulting interpretation would, therefore, be that subsection (b) refers to allocation of "charges, fees, rentals, and deposits" among various classes of customers. In Bee Cave's appeal case, Judge Card acknowledged the need to read the sections of §49.2122 together in stating:

> "[A]lthough that subsection itself [49.2122(b)] does not contain the phrase 'among classes of customers,' it exists in the context of a section that pertains to the establishment of customer classes. It's reference to 'charges, fees, rentals and deposits' is identical to the language in subsection (a), which explicitly governs differences among customer classes. That context and language raise questions concerning the scope and meaning of the subsection.

> The legislative history, set out by Appellants' briefs, supports the narrower interpretation they espouse."[7]

A copy of Judge Card's order addressing the applicability of §49.2122 is attached as Exhibit 1.

E. Prior Commission Interpretation

The Commission itself understood §49.2122 to refer only to customer class allocation. The Commission's legislative wrap-up report from the 80th legislative session states, on page 34, that under §49.2122 "*customer classes and* ***associated charges per class*** are presumed to be appropriate unless it is found that the district acted arbitrarily."[8] The Commission's notices regarding the rulemaking to implement the statute (an amendment to TCEQ's 30 TAC §291.41) contains similar language indicating that §49.2122 was limited to customer class issues. The public notice of TCEQ's January 16, 2008 agenda in which it first authorized publication of a proposed amendment to 30 TAC 291.41 to address the requirements of §49.2122 identified the purpose of the proposed rule change as solely to "allow a district to establish different utility rates among classes of customers." The notice of proposed rulemaking issued in the Texas Register on February 1, 2008 notes that §49.2122, which was part of Senate Bill 3, "allows a district to establish different charges, fees, rentals, or deposits among classes of customers that are based on any factor the district considers appropriate. These factors include the similarity of the type of customer to other customers; the type of service provided; the cost of facilities and operations including additional costs for security, recreational facilities, or fire protection; and/or the total revenue, including ad valorem tax revenues and connection fees received from a particular class of customers."[9] The notice of adoption of 30 TAC §291.41 issued in the Texas Register on July 4, 2008 also states that §49.2122 "allows a district to establish different charges, fees, rentals, or deposits among classes of customers based on any factor the district considers appropriate, including the factors listed in TWC, §49.2122(a), unless the district has acted arbitrarily or capriciously."[10] The Commission's interpretation limiting §49.2122 to customer class allocation issues is consistent with the legislative history and proper rules of statutory

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[7] Order No. 3 at p. 2, SOAH DOCKET NO. 582-08-2863, TCEQ DOCKET NO. 2008-0093-UCR (March 26, 2009)
[8] Legislative Wrap-Up Report, 80th Texas Legislature at p. 34 (2007): http://www.tceq.state.tx.us/comm_exec/igr/leg80.html.
[9] See http://texinfo.library.unt.edu/texasregister/html/2008/feb-01/PROPOSED/30.ENVIRONMENTAL.html#183.
[10] See http://texinfo.library.unt.edu/texasregister/html/2008/jul-04/index.html.

construction. Significantly, for purpose of the certified questions, the Commission's prior interpretation conflicts with the novel and unsupported interpretation advanced by LCRA and the Executive Director asserting that §49.2122 affected a fundamental change in the burden of proof in rate appeals that would limit the Commission's ability to ensure that water and wastewater utility rates are just and reasonable.

F. Harmonizing §§49.2122 and 13.043(j)

Section 13.043(j) places a statutory duty on the Commission in a rate appeal to "ensure that every rate made, demanded, or received by any retail public utility or by any two or more retail public utilities jointly shall be just and reasonable." In effect, this provision requires that a retail public utility, such as LCRA, demonstrate that its requested rates are just and reasonable, because the Commission is certainly not in a position to do so not being in possession of the relevant information.[11] Indeed, the Commission, in accordance with its obligations under §13.043(j), adopted 30 TAC §291.12 which clearly places the burden of proof in a rate proceeding on the provider of water and sewer services, including districts. After establishing the Commission's duty to ensure that retail public utility rates are just and reasonable, §13.043(j) goes on to say that, "*[R]ates shall not be unreasonably preferential*, prejudicial, or discriminatory *but shall be* sufficient, equitable, and *consistent in application to each class of customers.*" This sentence, phrased in the negative, provides a far less demanding requirement regarding application of rates to various customer classes.

If §49.2122(b) relieves a district of its burden of proof to establish that its rates are just and reasonable until a petitioner first presents a showing that the district acted arbitrarily and capriciously in setting its rates, the Commission would be prevented from fulfilling its obligation to *ensure just and reasonable rates* as required by Tex. Water Code §13.043(j). This overly broad interpretation would have the Commission simply *presume* that the rates were just and reasonable instead of having the Commission *ensure* that the rates are just and reasonable. In this situation, the Commission would not have met its statutory duty. This would be a direct conflict

[11] In its Reply to the Administrative Law Judges' Request for Answers to Certified Questions at p. 6 (May 6, 2009), LCRA attempts to argue that there is no statutory basis for LCRA to carry the burden of proof in appeals of its rates; however, the Commission has always previously required districts to carry the burden of proof in rate appeals, given the direction of Section 13.043(j).

between Tex. Water Code §13.043(j) and §49.2122(b). In the event of such a conflict, Section 13 of the Water Code would prevail. §49.002 of the Texas Water Code provides as follows:

> (a) Except as provided by subsection (b), this chapter applies to all general and special law districts *to the extent that the provisions of this chapter do not directly conflict with a provision in any other chapter of this code* or any Act creating or affecting a special law district. (emphasis added)

Because of this provision, any overly broad interpretation of §49.2122 would render that section inapplicable. This, however, is an undesirable result because we must presume that "the Legislature intends an entire statute to be effective and that a just and reasonable result is intended." *Helena Chemical,* S.W. 3d at 493.

If subsection (b) is limited simply to establishment of an initial hurdle prior to allowing a challenge to ***rate allocation*** among classes, then it would not conflict with the first sentence of Tex. Water Code §13.043(j). The second sentence of Tex. Water Code §13.043(j), which refers to customer classes, does not contain the same language requiring the commission to ***ensure*** that the rate classes are fair. Rather, the first part of this sentence is phrased negatively, in terms of what the rates must not be. It implies that there are many possible outcomes in rate design among classes so long as the rate design is **not** "unreasonably preferential, prejudicial, or discriminatory." Given the phrasing of the language here, it is reasonable that subsection (b) could exist without conflict when read as recommended by Bee Cave – to only apply to rate allocation among classes. The interpretation supported by Bee Cave allows, therefore, for a perfectly reasonable reconciliation between §13.043(j) and §49.2122(b).

2. Does Texas Water Code Section 49.2122(b) create a presumption that rates set by a district are properly established absent a showing that the district action setting the rates was arbitrary and capricious?

No. As Bee Cave explains above in response to Question No. 1, Texas Water Code §49.2122(b) does not create a presumption a district's rates are properly established, *i.e.*, just and reasonable, absent a showing that the action of setting the rates was arbitrary and capricious. An affirmative to this question would require us to assume that the statute in question refers to a determination of whether a district's rates are "just and reasonable." However, the term "just and reasonable" appears nowhere in §49.2122 despite the fact that it is a very commonly used term

discussed at great length in many Texas court decisions. The Texas Supreme Court in *Public Utility Com'n of Texas v. Houston Lighting & Power Co.*, 748 S.W.2d 439, 441 (Tex. 1987) stated: "It is generally recognized that the establishment of ***just and reasonable*** rates requires consideration of three factors: (1) the utility's reasonable and prudent operating expenses; (2) the rate base; and (3) a reasonable rate of return. *Railroad Commission of Texas v. Entex, Inc.*, 599 S.W.2d 292, 294 (Tex.1980); *Railroad Commission of Texas v. Houston Natural Gas Co.*, 289 S.W.2d 559, 573 (Tex.1956); Tex. Rev. Civ. Stat. Ann. art. 1446c, §39." (emphasis added). These three items are all components of the *revenue requirements* of a rate, the focus of Bee Cave's challenge to LCRA's rates.

The language of subsection (b) does not refer to any of these factors, and the term "just and reasonable" is simply ***not there***. Further, there is no mention of revenue requirements. Subsection (b) merely discusses whether a district "*properly established* charges, fees, rentals, and deposits and must be read in context with subsection (a) which authorizes the establishment of different charges, fees, rentals and deposits among customer classes." Had the legislature intended to address in subsection (b) a burden shift in determining whether a district's rates were just and reasonable, the legislature could have easily so stated. This absence of statutory language evidencing a legislative intent to affect a fundamental change in the burden of proof in ratemaking proceedings was noted by Judge Card in Order No. 3:

> "LCRA notes that its rate increase, as with any overall rate change, does pertain to customer classes. While technically this is true, the ALJ cannot help but think that the Legislature would more clearly explain its meaning if it intended for LCRA and other districts to be immune from any rate appeals unless they were shown to be arbitrary and capricious."[12]

It is also important to consider that an affirmative response to this question would dramatically change the law regarding the review of district-set rates. The repercussions of this change would affect retail water and sewer customers in every district in the state, and every wholesale purchaser of water or services from districts. Even LCRA acknowledges, in its Reply to the Administrative Law Judges' Request for Answers to Certified Questions at p. 7, that other

[12] Order No. 3 at p. 3, SOAH DOCKET NO. 582-08-2863, TCEQ DOCKET NO. 2008-0093-UCR (March 26, 2009)

districts are interested in this issue. There are well over ***1,000*** districts covered by §49.2122, providing services to millions of customers.[13] These customers, who previously could force a district to prove that its charges were just and reasonable if they could obtain petitions from more than ten percent of affected customers, could now face an inappropriate burden of having to prove that the district acted arbitrarily and capriciously in setting the rates. Traditionally, the burden has been placed on the utility to show that its rates are just and reasonable because only the utility has the detailed information (costs, customers, asset values, etc.) needed to establish a rate. Individual customers or a group of customers will seldom have the resources needed to review the district's cost data (which the district is not required to maintain in any accessible form), especially not for a district of the size and complexity of LCRA.

The effect of an affirmative response to this question, moreover, would not be limited to water and wastewater rates. Such a change would also apply to electric and electric transmission rates, and could affect the jurisdiction of the Public Utility Commission of Texas. LCRA, as a district, sells electricity on a wholesale basis and provides wholesale electric transmission service throughout the state. LCRA, as a river authority, is under the original jurisdiction of the PUCT.[14] The "charges, fees, rentals or deposits" addressed by §49.2122 are not limited to water and sewer charges. These certified questions also are not limited on their face to water and sewer rates. If §49.2122 applies to a district's water rates, it must also apply to a district's electric and electric transmission rates. The PUCT appears to be unaware that §49.2122 applies to river authorities because the PUCT has not adopted rules implementing §49.2122. The Commission should ensure that §49.2122 is applied consistently by the two agencies – otherwise, one set of customers (water and sewer) could eventually subsidize another set of customers.

Furthermore, this certified question proceeding does not offer an adequate opportunity for potentially affected parties to comment on the Commission's proposed action, given the potential magnitude of the change in the law that could result from the Commission's affirmative answer to this question. Such a proposed change should be subject to review and comment from all potentially affected parties, which could only be accomplished through rulemaking. Such a

[13] LCRA alone provides water and sewer services, including wholesale services, to more than 650,000 people. When electric services are considered, LCRA provides wholesale transmission service to all of the ERCOT service area, including more than 22 million retail electric customers.

[14] PURA defines "electric utility" to include river authorities. Tex. Util. Code §31.002(6). As an electric utility, LCRA is subject to the PUC's original jurisdiction. Tex. Util. Code §32.001.

proceeding would allow both districts and customers (and other affected agencies) to address these issues in a meaningful manner before the Commission.

The Executive Director may argue that additional rulemaking is not needed because the Commission adopted rules implementing §49.2122 in July 2008,[15] and that this question merely seeks an interpretation of those rules. Those rules, however, gave no indication that the changes made would dramatically change the ability of ratepayers to challenge district rates. The text of the rule parrots the statutory language, and the preamble states that the rule merely allows the district to establish different charges, fees, rentals or deposits.[16] No party commented for or against the amendment. Bee Cave asserts that the notice and reasoned justification provisions of the Commission's adoption of the rule were not sufficient if this rulemaking was broad enough to encompass a change in the law as broad as what would occur from an affirmative response to this question.

3. Does Texas Water Code Section 49.2122(b) only create a presumption that customer classes established by a district are properly established absent a showing that the district action establishing the classes was arbitrary and capricious?

Yes. As Bee Cave explains above in response to Question No. 1, Texas Water Code §49.2122(b) does not create a presumption that a district's *rates* are just and reasonable absent a showing that the action of setting the rates was arbitrary and capricious. Instead, the statute merely creates a presumption that classes with different rates are properly established absent a showing that the district action is arbitrary and capricious. In answering this question, Bee Cave assumes that the reference to customer classes would entail an assumption that the rates charged to different customer classes are indeed different. If the rates charged to different customer classes were not different, there would, of course, be no need to identify separate customer classes. The Clear Brook City Municipal Utility District case, SOAH DOCKET NO. 582-08-1700 is a perfect example of application of the statute for its intended purpose. The Clear Brook City MUD case concerns a rate classification dispute between Clear Brook City MUD and an apartment association. These are the same parties involved in an underlying rate classification dispute that led Representative Talton to file HB 2301 as indicated by his testimony presenting the bill before the House Natural Resources Committee and the sole testimony in support of that

[15] 33 Tex. Reg. 5327 (July 4, 2008), amending 30 TAC §291.41.
[16] 33 Tex. Reg. at 5329.

bill by a representative of Clear Brook City MUD.[17] In summary, that rate case appears to present the very issue that Tex. Water Code §49.2122 was enacted to address.

4. If the answer to Question No. 2 is YES, does Texas Water Code Section 49.2122(b) require the petitioner to make an initial showing that the district's rate-setting action was arbitrary and capricious?

Bee Cave's answer to Question No. 2 is NO; therefore, no further discussion should be required; however, if the Commission, against Bee Cave's recommendation, answers Question No. 2 with YES, then Bee Cave submits that the answer to this question would be YES; provided that the initial showing would be managed as follows:

1. The initial showing should be made before the administrative law judge assigned the case. Having the Commission make this determination prior to assignment would further slow down an already lengthy process.

2. The initial showing should not require a full hearing. The language of §49.2122(b) provides that there is a presumption "*absent a showing* that the district acted arbitrarily and capriciously." This statute does not mention a full shift of the burden of proof or a preponderance of the evidence standard. The statute, therefore, appears to contemplate only some initial hurdle, much like the requirement for a certain number of customer signatures to initiate the contested case process in which the district would still have the burden of demonstrating that its rates are just and reasonable. Further, if the burden required for a showing were the same as that of a hearing, then the parties would essentially be forced into having two hearings. Instead, the showing should be seen as only requiring a "prima facie" presentation of some evidence regarding *any* arbitrary and capricious actions. If the showing requires any more than that, ratepayers would face an almost impossible burden in challenging a district's rates.

3. The initial showing does not entail a complete shift of burden. Once the initial showing has been made and accepted, the district would retain its burden to demonstrate that its rates are just and reasonable.

[17] See Texas Legislature Online, 80th Regular Session, Video Broadcast: House Natural Resources Committee, March 28, 2007 at 1:14.

4. The initial showing may address any aspect of the rate-setting action, not just the procedural elements of the action. Additionally, the showing need not address every insufficiency of the rates. A showing that demonstrates that the districted acted arbitrarily and capriciously with respect to *any* aspect of the rates should be sufficient to shift the burden to the district to demonstrate that its rates are just and reasonable. Such a showing might address any of the following issues (or others): the district failed to use a historical test year in determining its rates, the district failed to rely on its own studies in determining its rates, the district used flawed accounting practices in determining its rates, or the district relied on flawed data in determining its rates. The reason Bee Cave requests this clarification (in the event the Commission answers Question No. 2 with YES) is that if the arbitrary and capricious standard were read to apply to only procedural requirements, no customer would every be able to challenge a district's rates if the district followed the relatively simple procedural steps needed to set its rates. Therefore, in such a situation, customers should be allowed to challenge any aspect of the rate-setting, procedural or otherwise, which indicates an arbitrary and capricious action.

Bee Cave also notes that if the showing discussed above were limited to cases where petitioners are challenging, not the revenue requirements, but only the allocations among customers classes, it would be appropriate to apply the provisions above to the initial showing requirements. Bee Cave, of course, cautions against any substantive response to this question, as written, because the only correct response to this question is NOT APPLICABLE.

5. If the answer to Question No. 4 is YES, in the circumstance that there is no showing that the district action setting the rates was arbitrary and capricious and the rates are therefore presumed to be "properly established," is there any further inquiry required into whether the rates themselves are valid? If so, what is the standard under which the rates themselves must be judged?

Bee Cave's answer to Question No. 2 (upon which Question No. 4 is based) is NO; therefore, no further discussion should be required. However, if the Commission, against Bee Cave's recommendation, answers Question Nos. 2 and 4 with YES, then Bee Cave submits that the answer to this question would be NO (no further inquiry would be required), provided that the initial showing is handled as described in Bee Cave's response to Question No. 4 above. Bee

Cave, of course, cautions against any substantive response to this question because the only correct response to this question, as written, is NOT APPLICABLE.

6. If the answer to Question No. 2 is YES, is the petitioner required to make the initial showing the district's rate-setting action was arbitrary and capricious whether the rate affected is for retail service, wholesale service, or raw water?

Bee Cave's answer to Question No. 2 is NO; therefore, no further discussion should be required; however, if the Commission, against Bee Cave's recommendation, answers Questions No. 2 and No. 4 with YES, then Bee Cave submits that the answer to this question would have to be YES as well. Section 49.2122 contains no provision restricting its application to only retail rates; therefore, an overly broad interpretation may have broad application and unforeseeable consequences. Bee Cave, of course, cautions against any substantive response to this question because the only correct response to this question is NOT APPLICABLE.

VI. CONCLUSION

WHEREFORE, PREMISES CONSIDERED the City of Bee Cave respectfully requests that the Commission answer Question Nos. 1 and 2 negatively, thereby restricting the application of §49.2122 to only allocations among customer classes, as intended by the legislature.

Furthermore, Bee Cave requests that the Commission set these questions for consideration in an expeditious manner. The ratepayers in LCRA's West Travis County Regional System have been patiently waiting for the opportunity to have the Commission fulfill its duty to ensure that the rates for services provided by LCRA are just and reasonable. The LCRA benefits from further delay in resolution of this matter, particularly given that its rates will automatically jump by 25% in October. Bee Cave hopes that the Commission will bear that in mind in setting these questions for consideration.

Respectfully submitted,

Jim Mathews
State Bar No. 13188700
Mathews & Freeland, L.L.P.
P.O. Box 1568
Austin, Texas 78768-1568
Phone: (512) 404-7800
Fax: (512) 703-2785

By: _____
Jim Mathews

ATTORNEY FOR CITY OF BEE CAVE

CERTIFICATE OF SERVICE

This is to certify that the undersigned sent a true and correct copy of the foregoing *Bee Cave's Brief in Opposition to Request for Answers to Certified Questions* in accordance with the applicable agency rules, as noted below, on this 12th day of June, 2009 to the following parties:

Christina Mann
Eli Martinez
Office of Public Interest Counsel
TCEQ, MC 103
P.O. Box 13087
Austin, Texas 78711-3087
Telephone: 512-239-6363
Fax: 512-239-6377

Christiaan Siano, Shana L. Horton
Environmental Law Division
TCEQ, MC 173
P.O. Box 13087
Austin, Texas 78711-3087
Telephone: 512-239-0600
Fax: 512-239-0606

Randall B. Wilburn
Attorney at Law
7408 Rain Creek Parkway
Austin, Texas 78759
Telephone: (512) 535-1661
Fax: (512) 535-1678

The Honorable Henry D. Card
The Honorable William Newchurch
The Honorable Kerrie Jo Qualtrough
Administrative Law Judges
State Office of Administrative Hearings
P. O. Box 13025
Austin, Texas 78711-3025
Telephone: 475-4993
Fax: 475-4994

James Rader and Sheridan G. Thompson
Lower Colorado River Authority
P.O. Box 220
Austin, Texas 78767-0220
Telephone: 512-473-3559
Fax: 512-473-4010

LaDonna Castañuela
Office of the Chief Clerk
TCEQ, Mail Code 105
PO Box 13087
Austin, TX 78711-3087

Dylan B. Russell
Hoover, Slovack LLP
5847 San Felipe, Suite 2200
Houston, Texas 77057
Telephone: (713) 977-8686
Fax: (713) 977-5395

Paul C. Sarahan
Fulbright & Jaworski LLP
1301 McKinney, Suit 5100
Houston, Texas 77010
Fax: (713) 651-5246

Georgia N. Crump
Lloyd, Gosselink, Rochelle & Townsend, P.C.
816 Congress Avenue, Suite 1900
Austin, Texas 78701
Telephone: (512) 322-5800
Fax: (512) 472-0535

Les Trobman
General Counsel
TCEQ, MC 173
P.O. Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-5525
Fax: (512) 239-5533

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Jim Mathews

EXHIBIT 1

SOAH DOCKET NO. 582-08-2863
TCEQ DOCKET NO. 2008-0093-UCR

APPEAL OF THE RETAIL WATER AND WASTEWATER RATES OF THE LOWER COLORADO RIVER AUTHORITY	§ § § § §	**BEFORE THE STATE OFFICE OF ADMINISTRATIVE HEARINGS**

ORDER NO. 3

The parties have filed briefs regarding burden of proof, standard of proof, and the applicability of TEX. WATER CODE ANN. §49.2122(b) to this rate appeal. The Administrative Law Judge (ALJ) agrees with Appellants that §49.2122(b) does not require them to prove that Lower Colorado River Authority (LCRA) acted arbitrarily and capriciously in establishing the rates at issue in this proceeding. The ALJ concludes LCRA has the burden of proving its rates are just and reasonable under Chapter 13 of the Water Code and Chapter 291 of the Texas Administrative Code. The ALJ concludes that this matter should proceed to a single-phase evidentiary hearing. The parties shall attempt to establish a procedural schedule accordingly.

TEX. WATER CODE ANN. §49.2122(b) states:

> Sec. 49.2122. ESTABLISHMENT OF CUSTOMER CLASSES.
> (a) Notwithstanding any other law, a district may establish different charges, fees, rentals, or deposits among classes of customers that are based on any factor the district considers appropriate, including:
> (1) the similarity of the type of customer to other customers in the class, including:
> (A) residential;
> (B) commercial;
> (C) industrial;
> (D) apartment;
> (E) rental housing;
> (F) irrigation;
> (G) homeowner associations;
> (H) builder;
> (I) out-of-district;
> (J) nonprofit organization; and

(K) any other type of customer as determined by the district;
(2) the type of services provided to the customer class;
(3) the cost of facilities, operations, and administrative services to provide service to a particular class of customer, including additional costs to the district for security, recreational facilities, or fire protection paid from other revenues; and
(4) the total revenues, including ad valorem tax revenues and connection fees, received by the district from a class of customers relative to the cost of service to the class of customers.
(b) A district is presumed to have weighed and considered appropriate factors and to have properly established charges, fees, rentals, and deposits absent a showing that the district acted arbitrarily and capriciously.

All the parties concede that LCRA is a "district" within the meaning of the statute. LCRA and the Executive Director contend that the plain language of subsection (b) requires a showing that LCRA acted arbitrarily and capriciously in establishing the rates that are the subject of this appeal. Consequently, they argue, the Appellants have the preliminary burden of proving those rates to have been set arbitrarily and capriciously. Only if the Appellants make such a showing would LCRA be required to prove the rates just and reasonable.

The City of Bee Cave, West Travis County MUD Nos. 3 and 5, and the Office of Public Interest Counsel (OPIC) contend, to the contrary, that Section 49.2122 applies only to the establishment of different rates among customer classes, as was the case in *Petition of Ratepayers Appealing Rates Established by Clear Brook City Municipal Utility District*, SOAH Docket No. 582-08-1700, TCEQ Docket No. 2008-0091-UCR. In that case, the ALJ's Order No. 6 concluded that Petitioners were required to make a preliminary showing that the rates were arbitrary and capricious. They contend that the statute is, at best, ambiguous, and that the legislative history plainly shows that this section was not intended to apply to general rate appeals.

The ALJ agrees with Appellants that the meaning of Section 49.2122(b) is ambiguous. Although that subsection itself does not contain the phrase "among classes of customers," it exists in the context of a section that pertains to the establishment of customer classes. Its reference to "charges, fees, rentals and deposits" is identical to the language of subsection (a), which explicitly governs differences among customer classes. That context and language raise questions concerning

the scope and meaning of that subsection. The legislative history, set out in Appellants' briefs, supports the narrower interpretation they espouse.

LCRA notes that its rate increase, as with any overall rate change, does pertain to customer classes. While technically that is true, the ALJ cannot help but think that the Legislature would more clearly explain its meaning if it intended for LCRA and other districts to be immune from any rate appeals unless they were shown to be arbitrary and capricious.

The ALJ concludes TEX. WATER CODE ANN. § 49.2122(b) does not require Appellants to prove that LCRA acted arbitrarily and capriciously in establishing the rates that are the subject of this appeal. He concludes LCRA has the burden of proving its rates to be just and reasonable. He further concludes that this matter should proceed to a single-phase evidentiary hearing.

The parties shall confer to determine an agreed procedural schedule for this proceeding. LCRA shall file that schedule by **April 7, 2009**. If the parties cannot agree, they shall file their individual schedule proposals by that date.

SIGNED March 26, 2009.

HENRY D. CARD
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

MATHEWS & FREELAND, LLP L.L.P.

ATTORNEYS AT LAW
P.O. Box 1568
Austin, Texas 78767-1568

Jim Mathews
Joe Freeland

(512) 404-7800
FAX: (512) 703-2785

Fax

To:	Company	Fax
LaDonna Castañuela	Chief Clerk, TCEQ	**239-3311**
Honorable Henry D. Card	SOAH	**475-4994**
Honorable William Newchurch	SOAH	-same-
Honorable Kerrie Jo Qualtrough	SOAH	-same-

From:	Fax	Phone
Jim Mathews	512/703-2785	512/404-7800

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Reference: SOAH Docket No. 582-08-2863; TCEQ Docket No. 2008-0093-UCR;
Appeal of the Retail Water and Wastewater Rates of the Lower Colorado River Authority;
***BEE CAVE'S BRIEF ON CERTIFIED QUESTIONS*; (1589.00; 4.1)**

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